

# Fiscal Note

*Fiscal Services Division*



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**SF 2100** – College Savings Accounts by Nonprofit and Community Foundations (LSB 5838XS)  
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Fiscal Note Version – New

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## **Description**

**Senate File 2100** adds tax-exempt, nonprofit organizations qualified under Internal Revenue Code (IRC) section **501(c)(3)** to the definition of “participant” for the **Iowa Educational Savings Plan Trust**. The Trust is also known as the Iowa College Savings 529 Plan. This action will allow these organizations to open and fund accounts for individual beneficiaries. The bill is effective July 1, 2016.

## **Background**

The Iowa College Savings 529 Plan (529 Plan) is Iowa’s version of a federally approved, tax advantaged college savings and finance program. The 529 Plan is administered by the Office of the State Treasurer. At the federal tax level, contributions to the 529 Plan are not tax advantaged, but assets grow tax free and withdrawals are tax free as long as the withdrawals are used for approved higher education expenses. Iowa provides an additional tax benefit by allowing contributions to be deducted from Iowa income tax, up to an annual maximum per taxpayer and per beneficiary. The Iowa deduction limit for tax year 2016 is \$3,188 and that amount is annually adjusted for inflation.

According to IRC section 501(c)(3), to qualify an organization must meet the following definition:

“Corporations, and any community chest, fund, or foundation, organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary, or educational purposes, or to foster national or international amateur sports competition....., or for the prevention of cruelty to children or animals, no part of the net earnings of which inures to the benefit of any private shareholder or individual,.....”

Organizations that are approved by the Internal Revenue Service under section 501(c)(3) are generally exempt from state and federal income taxation, although it is possible that some activities of such an organization will be subject to income tax. Contributions made by taxpayers to approved section 501(c)(3) organizations are deductible from state and federal taxable income.

## **Assumptions**

The Department of Revenue identified two potential tax situations where this bill could have a fiscal impact on the State General Fund. In both instances, the impact is expected to be minimal.

- Distributions from the 529 Plan may be used for a wider array of college expenses than traditional college scholarships and some scholarship distributions end up as taxable income for the student receiving the scholarship. Distributions from the 529 Plan are not taxed. If nonprofit organizations that currently provide higher education scholarships switch to the 529 Plan and away from traditional scholarships, income subject to the state income tax will decrease.

- While the income of nonprofit organizations is generally exempt from income tax, some organizations do engage in activities that produce taxable income and that income is subject to tax. If a qualified nonprofit organization that does have taxed income is able to use the 529 Plan contributions as a tax deduction, then State General Fund revenue would be negatively impacted.

In addition to the two minimal fiscal impacts identified by the Department of Revenue, this bill poses an additional, potentially significant fiscal impact. While the contributions to the 529 Plan by the nonprofit organizations provide no significant tax benefit to the organization, since the organization itself is generally exempt from income tax, the individuals contributing to the organization receive an income tax deduction for their contribution to the organization.

If this form of 529 Plan participation leads Iowa taxpayers to contribute more to tax-exempt, nonprofit organizations in order to support the organizations' college finance function, then income subject to state income tax will decline. For taxpayers in Iowa's highest income tax bracket (8.98%), every \$1.1 million to \$1.8 million in additional Iowa income tax deduction reduces net State General Fund revenue by \$100,000.

### **Fiscal Impact**

The addition of IRC section 501(c)(3) organizations to the definition of eligible participants in Iowa's 529 Plan has a potential negative fiscal impact on the State General Fund. That impact will occur if this change causes the overall contribution level of Iowa taxpayers to nonprofit organizations to increase. Such a situation could develop if Iowa taxpayers increase their charitable contributions in order to support the goals of the nonprofit 529 Plan participants made newly eligible under this bill. The Legislative Services Agency will continue to work with the Department of Revenue and the State Treasurer's Office to analyze this potential fiscal impact.

Other potential fiscal impacts were analyzed and determined to be minimal.

### **Sources**

Iowa Department of Revenue  
Legislative Services Agency analysis

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/s/ Holly M. Lyons

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The fiscal note for this bill was prepared pursuant to [Joint Rule 17](#) and the Iowa Code. Data used in developing this fiscal note is available from the Fiscal Services Division of the Legislative Services Agency upon request.

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